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DIRECTORATE OF INTELLIGENCE

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Japan: Debating New Loans to Mexico

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Summary

As its financial troubles have worsened, Mexico has begun to view Japan, which courted the Mexicans actively during their boom years in oil production, as an increasingly important source of funds. Mexico City has requested that Tokyo provide \$1 billion in project loans, but Japanese willingness to do so depends on a number of factors--including the attitude of the United States and the ability of the Mexican Government to come to an agreement on a balance-of-payments support package with the IMF. In our judgment, Mexico's large oil reserves and its proximity to the crucial US market will work in Mexico's favor as the Japanese consider the \$1 billion request. The Japanese have already agreed to fund some of the proposed projects, but we do not expect quick action on the remainder.

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This memorandum was prepared by Office of East Asian Analysis. Information available as of 16 June 1986 was used in its preparation. Comments and queries are welcome and may be directed to the Chief, Japan Branch, Northeast Asia Division, OEA

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Mexico Looks to Japan

The Mexican Government is seeking new sources of funds to help it cope with a shortage of foreign exchange exacerbated by the recent fall in oil prices. According to our most recent estimate, Mexico's net new money requirements--that is, new loans to cover their financial needs--for 1986 may surpass \$8 billion if oil prices remain low. Mexico sees Japan--with a current account surplus expected to reach \$75-80 billion in 1986--as a likely source of such funds. Moreover, the Japanese hold almost one-fifth of outstanding Mexican debt, making them the country's second most important creditor.

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[REDACTED] the key reason for the April trip to Tokyo by Mexican Finance Minister Silva Herzog was to seek a commitment of \$1 billion in new bilateral credits from Japan. Officially, Mexico is looking for funding for three projects--\$500 million for the Pacific Pipeline Project, \$250 million for the SICARTSA steel plant, and the remainder for an export development program--but Mexico City probably hopes to redirect some of the funds to help with its cash-flow troubles. The Export-Import Bank of Japan (EXIM Bank), a semi-independent government lending institution, would provide about 70 percent of the money and the rest would come from private Japanese banks. [REDACTED]

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Lender Attitudes Divided

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The current ambivalence within the Japanese Government about making new loans to Mexico is mirrored by similar uncertainty on the part of commercial banks. Although not enthusiastic about increasing debt exposure in Mexico (see figure 1), Japanese banks appear ready to provide more funds to help prevent Mexico from sliding into a default situation

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Outlook

Notwithstanding the current reluctance to extend new loans to Mexico, we believe that Tokyo will probably provide additional funding if Mexico City reaches an agreement with the IMF on a comprehensive package to provide balance-of-payments support. Japanese officials apparently believe that additional loans, if not accompanied by major reforms along the lines suggested by the IMF, would do little or nothing to enhance Mexico's ability to repay its existing debts. In our view, the project most likely to receive Japanese funding if Mexico and the IMF come to terms is the Pacific Pipeline. Despite the fall in oil prices, the pipeline remains attractive to Tokyo, which is still intent on diversifying Japan's sources of energy. An announcement would probably be timed to coincide with de la Madrid's visit to Tokyo, now projected for this fall.

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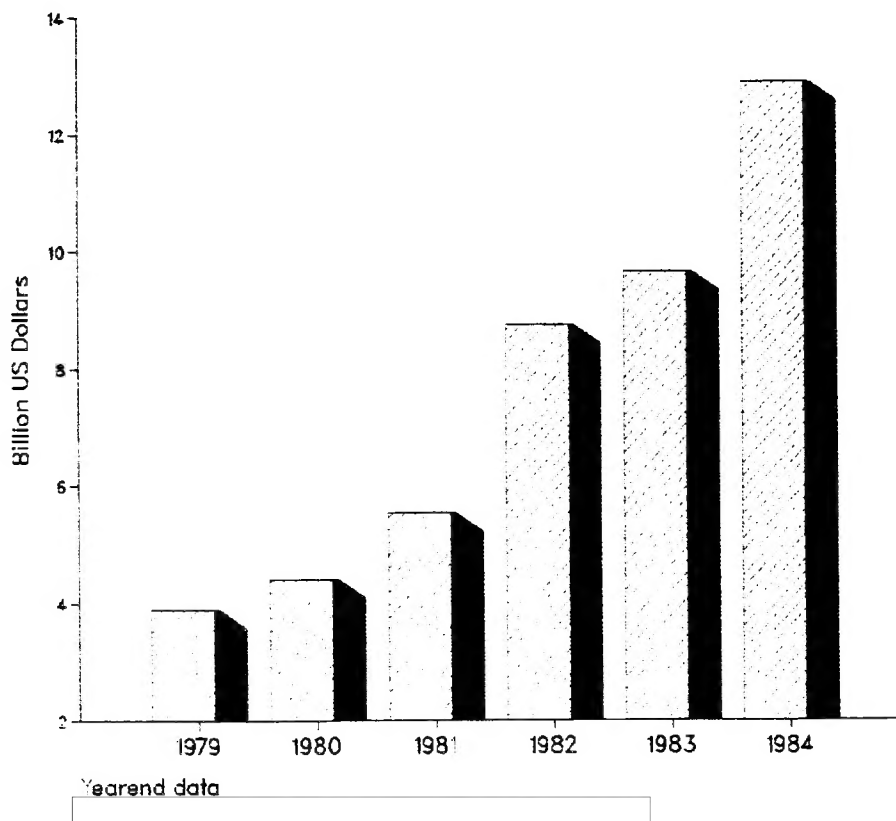
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Japanese Commercial Banks: Outstanding Loans to Mexico



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Even with an IMF agreement in hand, Tokyo's willingness to comply fully with the Mexican requests will be influenced by Washington's actions regarding the Mexican debt. (Mexican officials recognize this linkage, according to a recent US Embassy Tokyo cable.) Tokyo in recent months has indicated willingness to boost aid to countries of strategic interest to the United States to ease bilateral trade tensions, [REDACTED]

[REDACTED] Under the guise of supporting US interests, Tokyo in our view will probably provide substantial sums only to countries that it views as important to its economic interests. The most recent example of this is the Philippines, which Tokyo considers a part of its Asian backyard and to which the Japanese Government promised generous aid--to complement US funding--when President Aquino assumed office. Although the Japanese Government has only reluctantly supported US initiatives in Central America--for example, by dragging its feet on reopening its Embassy in El Salvador despite repeated requests by Washington-- Tokyo may be willing to play ball in Mexico. The country's large oil reserves, its proximity to the crucial US market, and the admittedly long-term prospect for sustained economic growth probably place Mexico on Tokyo's small list of countries considered "strategic." [REDACTED]

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